Supreme Court, U.S.
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No. _____

In The

Supreme Court of the United States

LINDSEY SPRINGER, d/b/a
BONDAGE BREAKER MINISTRIES,

Petitioner,

v.

UNITED STATES SECURITIES AND
EXCHANGE COMMISSION, et al.,

Respondent.

On Petition For Writ Of Certiorari To The United States Court Of Appeals For The Third Circuit

PETITION FOR WRIT OF CERTIORARI

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78 pp

QUESTION(S) PRESENTED

1. Whether the known fact three different Circuit Courts of Appeals are divided as to the meaning of the undefined term "Investment Contract," after the holding by this Court in *S.E.C. v. Howey*, demands this Court revisit its posture and clarify what Congress has failed or refused to adopt in over 55 years since that decision?

2. Does the rule of lenity apply in civil fraud cases?

3. Whether the Common Enterprise test judicially created by this Court's Decision in *S.E.C. v. Howey* is so vague that it requires this Court to redefine what it intended to mean since Congress refuses to offer any legislative meaning for the term "Investment Contract?"

4. Whether the term "Investment Contract," when used to enforce the Security Laws of 1933 and 1934, violates the due process clause of the Fifth Amendment where property belonging to Petitioner was taken by the United States under the claim of registration violations?

5. Whether the Securities and Exchange Commissions' enforcement of the registration provisions of the Security Act of 1933 and the Securities and Exchange Act of 1934, involving the definition of Security, is Unconstitutionally vague as it does not provide a definition for the term "Investment Contract?"

6. Whether Congress can legitimately claim a power to regulate under its Commerce Power certain "Investment

QUESTION(S) PRESENTED – Continued

Contracts," without providing the public what the meaning of that term intends to mean?

7. Whether the term "Investment Contract," identifying a type of Security covered by the Security Acts of 1933 and 1934, without more definition, is an unenforceable provision contained within the registration provisions of the Acts?

8. Whether private trust associations who enter into agreements with its members are subject to the Security Acts of 1933 and 1934?

9. Whether Congress' refusal to act in over 55 years regarding this Court's Holding of the meaning of the term "Investment Contract," in *S.E.C. v. Howey*, is sufficient enough to show Congress intends not to define the term "Investment Contract," and that the term should be ordered Unconstitutional and unenforceable?

10. Whether the fact three different Circuit Courts of Appeals have published opinions which oppose each other on the meaning of the term "Investment Contract," is ample reason for this Court to revisit its holding in *S.E.C. v. Howey*?

11. Whether this Court should remand this Case back to the Third Circuit with directions consistent with this Court's revisitation of *S.E.C. v. Howey*?

LIST OF PARTIES

All parties do not appear in the caption of the case on the cover page. A list of all parties to the proceeding in the court whose judgment is the subject of this petition is as follows:

The Infinity Group Company;
Geoffrey P. Benson;
Geoffrey J. O'Connor;
Futures Holding Company;
SLB Charitable Trust;
Susan L. Benson;
JGS Trust

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PETITION FOR WRIT OF CERTIORARI

Petitioner respectfully prays that a Writ of Certiorari issue in review of the judgment below.

OPINIONS BELOW

The orders of the United States District Court appear at Appendix to the petition, App. 40.

The orders of the United States Court of Appeals for the Third Circuit appear at Appendix to the petition, App. 1.

JURISDICTION

The date on which the United States District Court issued its final order; *February 6, 1998.*

The date on which the United States Court of Appeals for the Third Circuit Affirmed District Court's Order; *May 4, 2000.*

Petition for Rehearing *En Banc* was *denied on July 14, 2000.*

The jurisdiction of this Court is invoked pursuant to 28 U.S.C. § 1651(a).

CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

The Constitutional provision involved is Article I, Section 8, Cl. 3. The statutes include 15 U.S.C. § 77b(a)(1),

§ 77v, § 78u, § 78aa, and the Security Acts of 1933 and 1934.

THIS PETITION IS IN AID OF APPELLATE JURISDICTION

STATEMENT OF THE CASE

This case brings the issue of the meaning of the term "Investment Contract" and the obvious division amongst at least three different federal Circuits on the meaning of the term "Common Enterprise" to this Court's attention again. *Mordaunt v. Incomco*, 469 U.S. 1115, 1117 (1985).

"Horizontal" means pooling of funds with pro-rata distribution of profit and loss. *Steinhardt Group, Inc. v. Citicorp*, 126 F.3d 256 (3rd Cir. 1997). "Strict Vertical" means fortunes interwoven and mutually dependent. *Mordaunt v. Incomco*, 686 F.2d 815, 817 (9th Cir. 1982). "Broad Vertical" means profits must be tied to the promoters effectiveness and skill. *S.E.C. v. Continental*, 497 F.2d 516, 522-23 (5th Cir. 1974).

This case involves over 10,000 people loaning money to the Infinity Group Company Trust in exchange for receiving the pie in the sky minimum of 20% interest calculated from the loan amount, and in the sweetest portion of the pie, over 138% interest in 1 year and 75 days.

Title 15, § 77b(a)(1) defines the term "Security" to include a plethora of terms, one of which is "Investment Contract." If a person offers for sale an unregistered Investment Contract he is subject to 15 U.S.C. §§ 77v and 78u & 78aa.

The TIGC 20% interest was paid in the form of a waiver of the membership dues and the monthly newsletter being delivered without any other expense on the part of the member. Minimum loan was $1200.00. Membership dues and $169.00 annual subscription to newsletter were then paid to lender. Persons who loaned higher amounts were only offered the same as the person loaning $1200.00, save the amount of interest they could receive if the pie ever rose in the money oven.

Persons who only were willing to loan $100.00 were required to pay the monthly news letter fees and the membership fees. Basically, this person received no interest whatsoever unless their loan amount exceeded the $1200.00 minimum.

There is no question that any person who expects to receive more than the amount of interest they received in a FDLIC insured institution, must have known the risks involved in a contract agreement which had no such insurance. The more the lender expected above the normal prime, the greater the lender must have known the risks to be. This is just the common sense of this case.

A person with a 1 million dollar CD in a FDLIC insured institution is only insured to $100,000.00. The other $900,000.00 is just as at risk there as it is in any other financial scheme where a person needing to loan his money seeks persons who are needing to borrow same. Drilling an oil well comes to mind where the persons who loaned the money were only offered a possible interest return and did not share in the success or failure of the oil drilling venture.

Beginning April 2, 1997, the Security and Exchange Commission ("SEC") began a formal investigation of a

private membership ($169.00 to join) association referred to as The Infinity Group Company Trust ("TIGC") involving 10,000 people from every State in the Union and some territories of the U.S.

On August 26, 1997, the SEC commenced formal injunctive action in the Eastern District of Pennsylvania claiming against TIGC for violations of the Security Laws of both 1933 and 1934 ("the Acts") and also claimed against Lindsey K. Springer, d/b/a Bondage Breakers Ministries ("petitioner") **(as a mere "relief defendant" therein)** (solely on basis petitioner was in possession of ministry donations [$1.265 million] to which allegedly originated from the alleged conduct against TIGC), and that since petitioner had allegedly not given any consideration for this donation, although no wrong doing was alleged against petitioner, SEC claimed they could demand disgorgment of the allegedly unconsidered donation from petitioner because the money originated from the offer and sale of an unregistered security in the form of an investment contract.

On August 27, 1997, the SEC, among others, requested the district court appoint a Trustee to act on its behalf to account to the SEC what the current position of all property belonging to TIGC was and to take control and possession of all property belonging to those accused of Security Law violations. These violations consisted of failure to register a security with the SEC as well as alleged activation of the anti-fraud provisions governing the sale of a registered or unregistered security in the form of an investment contract.

At the preliminary hearings held on September 5, 2000, the Honorable Judge Dalzell made it perfectly clear

the investment contract to which the allegations of the SEC involved, was that of a capital unit or "share" as it was sometimes referred by the SEC and its employee witnesses. A final hearing was then scheduled requiring the SEC to convert their prima facia case to a level of preponderance. This hearing was originally scheduled for September 30, 1997, reaffirming and continuing Judge Brody's TRO.

On February 2, 1998, Judge Dalzell held final injunction hearing at which the SEC was allowed to present their preponderance case involving investment contract capital unit share securities. A cursory review of the many names the SEC referred to in their plethora of documents demonstrated the SEC had no idea what their power reached involving the activities of defendants and relief defendants.

As a secondary matter, the SEC alleged defendants had perpetrated a fraud upon the public involving the investment contract capital unit share securities. As a third matter, the SEC sought monetary relief against all relief defendants to which no wrongdoing was alleged. Disgorgement was the subject matter and only issue involving these relief defendants.

On February 5, 1998, after the SEC had rested and failed to establish the actual existence of the alleged capital unit security, appellee (and appellants) moved Judge Dalzell to dismiss the SEC's complaint on the grounds the Court lacked subject matter jurisdiction. This of course was denied by Judge Dalzell.

On February 6, 1998, Judge Dalzell issued his final order for the purpose of appeal which found that defendants had sold investment contract property transfer and agreement capital unit share securities to the public and

that disgorgement was appropriate involving all legal tender raised by defendants involving the unregistered sale of the investment contract property transfer agreement capital unit securities. Petitioner herein was ordered to judgment in excess of "$1.2 million" in legal tender. App. at 55.

On May 4, 2000, the Third Circuit Court of Appeals affirmed the lower court Judgment on the basis that to do otherwise would "embroider a loophole into the fabric of the securities laws by limiting the definition of 'securities' in a manner that unduly circumscribes the protection Congress intended to extend investors." App. at 19.

On July 14, 2000, the Third Circuit Court of Appeals denied the Petition for Rehearing and denied the Petition for Rehearing En Banc. App. at 20.

This appeal follows.

REASONS FOR GRANTING THIS WRIT

Congress has enumerated power to regulate Commerce among the several states to the Executive Branch involving the registration requirements of Securities by way of the Security Act of 1933 and the Exchange Act of 1934 ("the Acts"). The SEC regulates securities sold within the Commerce Power's jurisdiction.

Congress defined for the Executive Law Enforcer the term "security" to mean, among other specific terms, any investment contract. The Supreme Court has previously determined whether the investment contract in question was in fact regulatable by Congress within its Commerce

power in *S.E.C. v. Howey*, 328 U.S. 293. This decision determined that "[A]n investment contract for purpose of the Securities Act means a contract, transaction or scheme whereby a person invests his money in a common enterprise and is led to expect profit solely from the efforts of the promoter or a third party, it being immaterial whether the shares in the enterprise are evidenced by formal certificates or by nominal interests in the physical assets employed in the enterprise." *Id.* at 298-99

There is no question the United States Courts of Appeals are divided on the "common enterprise" elements required to invoke SEC regulatory demands under this holding. In 1995 Maura K. Monaghan wrote "An Uncommon State of Confusion" involving the Common Enterprise Element. 63 Fordham L. Rev. 2135, 2152-53 (1995).

The Third Circuit recently defined what a common enterprise need be in order to satisfy its "*Howey*" test. Specifically the second prong, which concluded the SEC may only regulate a investment contract if and only if it involves a "common enterprise" which is "horizontal."

The Third Circuit defined its "common enterprise" term in pertinent and applicable part that in order for a common enterprise to exist, the enterprise must distribute to its shareholders pro-rata, in essence dividing the losses and or excesses on an equal basis with the ratio of shares owned. *Steinhardt Group, Inc. v. Citicorp*, 126 F.3d 144, 151 (3rd Cir. 1997)

Although the Third Circuit said defendants sold "Capital Units," no evidence of a Capital Unit was ever entered into the record in the District Court.

The SEC could not, in discovery, produce any "capital unit" document, even though their progeny, Ohio Security Division, had seized all the documents contained by TIGC in Ohio. The SEC alleged 10,000 victims and yet could not produce one investment contract which could satisfy the *Howey* test, not to mention the *Steinhardt* test (3rd Cir.).

Relief defendants were entered judgment against well beyond their capabilities or involvement when no violation of the law was alleged. Petitioner received a donation for the purposes of expanding Petitioner's ministry and that if this judgment remains intact, churches and other religious organizations will be liable for past donations to the executive branch regardless of from whom or when donated on mere allegations of civil prima facia wrongdoing.

If a Federal Law is to mean it can only apply to Interstate Commerce in all 50 States Uniformly, then the term Investment Contract is violating this fundamental principle. Not only is this done by the Legislature for refusing to adopt this Court's holding in *Howey*, but furthermore, the Judicial Branch at both the Third, Fifth and Ninth Circuits are directly divided against one another on the meaning of this Court's term "Common Enterprise."

How can Common Enterprise mean one thing to a contract in commerce in one part of the country and mean something totally and undeniably different in another part of the country? Simply it cannot and should not be maintained in a Constitutional form of government.

This Court said in *Jones v. United States*, 529 U.S. ___ (2000), that "ambiguity . . . should be resolved in favor of lenity." at 9. Furthermore, "when choice has to be made between two readings of what conduct Congress has made a crime, . . . we choose . . . , to require that Congress should have spoken in language that is clear and definite." "Unless Congress conveys its purpose clearly, it will not be deemed to have significantly changed the federal-state balance." Although the Acts involved in this case are not criminal per se, they have criminal intentions, and criminal terms such as "fraud."

TIGC is not a common enterprise as recently defined by the Third Circuit Court in *Steinhardt v. Citicorp*, 126 F.3d 144 (3rd Cir. 1997). *S.E.C. v. Howey*, 328 U.S. 293-299 establishes the only way an investment contract may constitutionally be upheld to fall within Congress' Article 1, Section 8, Clause 3 Commerce power. This does not mean that a contract of some other sort does not qualify as an investment as that term is generally and randomly used.

CONCLUSION

Because the documents used by TIGC with its member/lenders did not distribute on a pro-rata basis, the property transfer and agreement document cannot be relied upon to establish the existence of a SEC regulated and required to be registered investment contract within the Third Circuit's recent definition of "common enterprise."

This Court should reverse the Third Circuit Court of Appeals and District Court and order return of property taken from petitioner on the basis alone that the district court did not have subject matter jurisdiction to hear in favor of the SEC on grounds no evidence exist and none was presented, demonstrating a security, in the form of an Investment Contract, anywhere within the district court's voluminous record and according to the law.

There is no question the Security Acts do not apply except to the regulation of Securities.

Because the term "Common Enterprise" is not defined by Congress and because three Circuits are divided on the meaning of the term "Common Enterprise," this Court should Grant this Writ of Certiorari.

Date: December 18, 2000

Respectfully submitted,

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App. 1

Filed May 4, 2000

UNITED STATES COURT OF APPEALS
FOR THE THIRD CIRCUIT

Nos. 98-1215, 98-1216, 98-1217

UNITED STATES SECURITIES AND
EXCHANGE COMMISSION,

v.

THE INFINITY GROUP COMPANY; GEOFFREY P. BENSON; GEOFFREY J. O'CONNOR; FUTURES HOLDING COMPANY; SLB CHARITABLE TRUST; SUSAN L. BENSON; JGS TRUST; LINDSEY SPRINGER; BONDAGE BREAKER MINISTRIES

LINDSEY SPRINGER;
BONDAGE BREAKER MINISTRIES,

THIRD-PARTY PLAINTIFFS

v.

THE UNION STATES OF THE CONSTITUTION, i.e.; ALASKA; ALABAMA; ARKANSAS; ARIZONA; CALIFORNIA; COLORADO; CONNECTICUT; DELAWARE; FLORIDA; GEORGIA; HAWAII; IOWA; ILLINOIS; INDIANA; KANSAS; KENTUCKY; LOUISIANA; MASSACHUSETTS; MARYLAND; MAINE; MICHIGAN; MINNESOTA; MISSOURI; MISSISSIPPI; MONTANA; NORTH CAROLINA; NORTH DAKOTA; NEBRASKA; NEW HAMPSHIRE; NEW JERSEY; NEW MEXICO; NEVADA; NEW YORK; OHIO; OKLAHOMA; OREGON; PENNSYLVANIA; RHODE ISLAND; SOUTH CAROLINA; SOUTH DAKOTA; TENNESSEE; TEXAS; UTAH; VIRGINIA;

VERMONT; WISCONSIN; WEST VIRGINIA; WYOMING; WASHINGTON; FEDERAL DISTRICT OF COLUMBIA,

THIRD-PARTY DEFENDANTS

Geoffrey J. O'Connor (98-1215), Geoffrey P. Benson (98-1216), Susan L. Benson, Pro Se on behalf of herself in her representative capacity on behalf of SLB Charitable Trust, Futures Holding Company and JGS Trust (98-1217),

Appellants

ON APPEAL FROM THE
UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF PENNSYLVANIA
Civil No.: 97-CV-05458
District Court Judge: Honorable Stewart Dalzell

Argued: March 2, 1999

Before: ALITO and MCKEE, *Circuit Judges*, and SCHWARTZ, District Judge*

(Filed: May 4, 2000)

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* The Honorable Murray M. Schwartz, Senior District Judge of the United States District Court for the District of Delaware, sitting by designation.

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OPINION OF THE COURT

McKEE, *Circuit Judge.*

Defendants appeal the grant of a permanent injunction in this civil action for securities fraud. The defendants argue that the instruments that they offered to

investors were not "securities" under federal law, and that the district court therefore lacked subject matter jurisdiction. The defendants also challenge certain evidentiary and procedural rulings that the district court made during the hearing on the motion for a permanent injunction. For the reasons that follow, we will affirm.

I.

In November 1995, defendants Geoffrey Benson and Geoffrey O'Connor formed the Infinity Group Company Trust (the "Trust" or "TIGC").[1] Thereafter, the Trust unveiled an "Asset Enhancement Program" that offered investors an opportunity to invest with the expectation of exceedingly high return and minimal risk. Investors in TIGC were asked to execute "property transfer contracts" pursuant to which the investors contributed substantial sums of money to the Trust for the Trust to invest. TIGC guaranteed investors that they would receive an annual rate of return ranging from 138% to 181% depending on the amount of the participant's principal investment.[2] The guarantees were based upon the Trust's purported performance experience, financial connections, and the ability to pool large amounts of money. Participants were promised that their principal would be repaid upon

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[1] Benson was the Executive Trustee Director of TIGC. O'Connor was also a trustee of TIGC. As Trustees of TIGC, Benson and O'Connor exercised sole discretion of the Trust's investment programs.

[2] For property transfers of $1,200 to $50,000, the guaranteed rate of return was 138%. For amounts greater than $50,000, the return rate was 181%.

demand. Once the property transfer contracts were executed, the transferred funds became assets of the Trust and were subject to investment at the sole discretion of the Board of TIGC.

TIGC's solicitation was successful. It raised approximately $26.6 million from over 10,000 investors nationwide. However, TIGC only invested $12 million of the funds it received pursuant to the property transfer contracts, and it never earned a profit on the funds it did invest.[3] Rather, the Trust sustained mounting loses [sic] that it failed to disclose to investors. The district court described what happened as follows:

> TIGC also used over $2 million in so-called downline commissions to keep the engine of this enterprise humming like a new Mercedes on the autobahn. In the time-dishonored tradition of Charles Ponzi, TIGC substituted new investors' money for real investment return on old investors' funds.
>
> The rest of TIGC's expenditures were even less investment-related. More than $816,000 was spent on real estate, a significant portion of which went to the purchase and development of a personal residence for Geoffrey and Susan Benson . . . the purchase or lease of cars for their garage, . . . a $6,133.46 spending spree at Circuit City; more than $2,000 spent at television

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[3] Defendants contend that the money that was not invested was used for "operating expenses" and charitable contributions or that it constituted "excess profits." Appellant's Br. at 11. The evidence at trial established that the money not invested was used to pay "dividends" to earlier investors and personal expenses of the Benson family. Appellee's Br. at 12-13.

> retailers; over $50,000 in 'household expenses'; $5,000 to pay off a home mortgage; $10,000 to pay off personal credit card bills; $10,000 for school tuition for the Bensons' son; as well as hundreds for jewelry, bowling equipment and membership fees, [sic] groceries. In short, the Bensons used TIGC as their personal checking account.
>
> In addition, Geoffrey Benson made an undisclosed donation of $1.265 million of investor funds to Lindsey K. Springer, d/b/a Bondage Breaker Ministries.
>
> In addition to all this, defendants Geoffrey Benson and Geoffrey O'Connor paid themselves nearly $300,000 in cash from TIGC's funds, none of it reported to the Internal Revenue Service or even documented on TIGC's books – which did not exist. Lastly, more than $1.9 million remains unaccounted for,. . . . [4]

SEC v. Infinity Group Co., 993 F.Supp. 324, 325-26 (E.D.Pa.1998) (original footnote omitted).

On August 27, 1997, the SEC filed the instant complaint in the United States District Court for the Eastern District of Pennsylvania charging "an ongoing scheme, directed by Benson and O'Connor, to defraud public

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[4] The district court agreed with the SEC's claim that the operation of the Trust was "the classic *modus operandi* of Ponzi schemes." Appellee's Br. at 21. For a brief explanation of the origin of "Ponzi schemes" and Charles Ponzi *see Bald Eagle Area School District v. Keystone Financial, Inc.*, 189 F.3d 321, 324 n. 1 (3rd Cir. 1999), and Mark A. McDermott, *Ponzi Schemes and the Law of Fraudulent and Preferential Transfers*, 72 Am. Bankr. L.J. 157, 158 (1998).

investors through the offer and sale of TIGC securities, in the form of investment contracts," App. 41a, in violation of Section 22 of the Securities Act of 1933, 15 U.S.C. 77v, and Sections 21 and 27 of the Securities Exchange Act of 1934, 15 U.S.C. 78u & 78aa. The Commission sought a permanent injunction, a freeze of the assets of TIGC, appointment of a Trustee to manage the affairs of TIGC, and an order requiring defendants, and certain third parties (the "relief defendants") to disgorge assets of TIGC that had been improperly transferred.[5]

On September 5, 1997, after a hearing, the district court issued an Order for Preliminary Injunction, Appointment of Trustee, and Freeze of Assets and Other Relief. Although the Trust's funds and assets were frozen, the September 5 Order provided for the release of funds to pay legal expenses and fees, as well as defendants' living expenses. On February 6, 1998, the district court entered a final judgment against the defendants enjoining them from further violations of the securities laws and ordering disgorgement of all amounts contributed to the Trust by the Trust participants. This appeal followed.

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[5] The SEC sought disgorgement from the following relief defendants: Futures Holding Company (controlled, in part, by Benson); SLB Charitable Trust (a charitable trust established in the name of Susan Benson, Benson's wife); Susan L. Benson (trustee of SLB and TIGC); JGS Trust (a "family trust" controlled by Benson); Lindsey Springer (manager and "legal representative" of TIGC and controller of Bondage Breaker Ministries); and Bondage Breaker Ministries.

II.

Defendants raise four issues on appeal. First, they argue that the property transfer contracts that were used as an "investment" vehicle here were not "securities" under federal securities laws, and therefore that the district court lacked subject matter jurisdiction. Second, they argue that inasmuch as they sincerely believed in the investments that TIGC made, there can be no liability for securities fraud. Third, they allege that the district court erred in denying their concededly untimely demand for a jury trial. Lastly, they contend that several allegedly erroneous procedural and evidentiary rulings constitute reversible cumulative error even though the rulings were harmless when considered separately. We will discuss each argument in turn.

III.

We must first address the defendants' claim that the district court lacked subject matter jurisdiction because the "property transfer contracts" were not "securities" under federal securities laws. Inasmuch as this is an appeal from a final judgment, we have jurisdiction to review the district court's decision under 28 U.S.C. § 1291. We exercise plenary review over a district's ruling on a motion to dismiss for lack of subject matter jurisdiction. *Delaware Valley Citizens Council v. Davis*, 932 F.2d 256, 264 (3d Cir. 1991).[6]

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[6] Although the district court treated defendants' motion to dismiss for lack of subject matter jurisdiction as a Rule 12(h)(3) motion, the parties here have treated it as a 12(b)(1) motion. We

It is well established that federal securities laws only apply to the purchase or sale of "securities" as defined therein. *Steinhardt Group Inc. v. Citicorp*, 126 F.3d 144, 150 (3d Cir. 1997).

> '[S]ecurity' means any note, stock, treasury stock, bond, debenture, evidence of indebtedness, certificate of interest or participation in any profit-sharing agreement, collateral-trust certificate, . . . *investment contract*, voting-trust certificate, . . . any interest or instrument commonly known as a 'security', or any certificate of interest or participation in, . . . or right to subscribe to or purchase, any of the foregoing.

15 U.S.C. § 77b(a)(1) (emphasis added). The property transfer agreements that TIGC's investors executed certainly appear to be "investment contract[s]," however "[t]he term investment contract has not been defined by Congress, nor does the legislative history to the 1933 and 1934 Acts illuminate what Congress intended by the term investment contract." *Steinhardt*, 126 F.3d at 150-51. In *SEC v. W.J. Howey Co.*, 328 U.S. 293 (1946), the Supreme Court provided a framework for determining when such agreements are subject to federal law. The Court stated:

> [A]n investment contract for purposes of the Securities Act means a contract, transaction or scheme whereby a person invests his money in a common enterprise and is led to expect profits solely from the efforts of the promoter or a third party, it being immaterial whether the shares in

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exercise plenary review under either. *See Nationwide Insurance Co. v. Patterson*, 953 F.2d 44, 45 (3d Cir. 1991) (Rule 12(h)(3) motion to dismiss is subject to plenary review).

> the enterprise are evidenced by formal certificates or by nominal interests in the physical assets employed in the enterprise.

Howey, 328 U.S. at 298-99. Thus, the property transfer contracts between TIGC and its investors are securities if they were (1) "an investment of money," (2) "in a common enterprise," (3) "with profits to come solely from the efforts of others." *Id.* at 301, *Steinhardt*, 126 F.3d at 151.

Defendants agree that the property transfer contracts satisfy the first and third prongs of the *Howey* test. Indeed, they can hardly deny it. There clearly was an investment of money because the contracts required and evidenced the monetary transfer solely for the purposes of receiving the "guaranteed" return of between 138% and 181%. *See Steinhardt*, 126 F.3d at 151 (finding prong one met where an investment was made with the expectation of an 18% return on investment). Similarly, the third prong is clearly satisfied here because the expected return was to be "with profits to come solely from the efforts of others." *Id.* (quoting *Howey*, 328 U.S. at 301).

Our focus under the third prong is whether "the purchaser [is] attracted to the investment by the prospect of a profit on the investment rather than a desire to use or consume the item purchased." *Id.* at 152. TIGC's investors did not intend to consume anything in return for the money they gave to TIGC. Whether the investor has "meaningfully participated in the management of the partnership in which it has invested such that it has more than minimal control over the investment's performance" is also relevant under the third prong. *Id.* TIGC concedes that "the TIGC Board retained exclusive control over the investment decision." Appellant's Br. at 18. Thus, the

participants were passive investors who exercised no control over the funds they gave to TIGC. Those investors depended upon the managerial decisions of others. Therefore, we agree that the first and the third prongs have been satisfied,[7] and we will focus our analysis upon the "common enterprise," or second prong, of the *Howey* test.

We have held that the common enterprise requirement is satisfied by "horizontal commonality."[8]

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[7] Even though the parties agree that the first and third prong are satisfied, we must independently satisfy ourselves that those prongs are established because the inquiry is jurisdictional, and we have an independent responsibility to insure that subject matter jurisdiction exists. *See Steel Company v. Citizens for a Better Environment*, 523 U.S. 83, 94 (1998) (federal courts must decide jurisdictional issues "even when not otherwise suggested, and without respect to the relation of the parties to it.").

[8] Circuit courts of appeals utilize two distinct approaches in analyzing commonality; "vertical commonality," and "horizontal commonality." "Vertical commonality" focuses on the community of interest between the individual investor and the manager of the enterprise. *See e.g., Long v. Acultz Cattle Co.*, 881 F.2d 129 (5th Cir. 1989) ("A common enterprise is one in which the fortunes of the investor are interwoven with and dependent upon the efforts and success of those seeking the investment or of third parties") (*quoting Glenn W. Turner Enterprises, Inc.*, 474 F.2d 476, 482 n.7 (9th Cir. 1973)). "Horizontal commonality" examines the relationship among investors in a given transaction, requiring a pooling of investors' contributions and distribution of profits and losses on a pro-rata basis. *See e.g., Salcer v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 682 F.2d 459 (3d Cir. 1982); *Cooper v. King*, 114 F.3d 1186 (6th Cir. 1997); *SEC v. Lauer*, 52 F.3d 667 (7th Cir. 1995).

In *Steinhardt*, we declined to decide if we should adopt a vertical commonality analysis when conducting an inquiry under the commonality prong of *Howey*. *Steinhardt*, 126 F.3d at

Horizontal commonality is characterized by "a pooling of investors' contributions and distribution of profits and losses on a pro-rata basis among investors." *Steinhardt*, 126 F.3d at 151 (*quoting* Maura K. Monaghan, *An Uncommon State of Confusion: The Common Enterprise Element of Investment Contract Analysis*, 63 Fordham L.Rev. 2135, 2152-53 (1995) (footnotes omitted)). *See also Salver v. Merrill Lynch, Pierce, Fenner & Smith*, 682 F.2d 459, 460 (3d Cir. 1982) (holding that a commodity account is not a "security" because it is not part of a pooled group of funds). Here, it is undisputed that TIGC's solicitation and membership materials stated that TIGC would pool participant contributions to create highly-leveraged investment power that would yield high rates of return while protecting the investors' principal contributions. For example, the Trust's Private Member Material and Manual represents:

> The Infinity Group Company invests for profit by accepting amounts as low as [$1200] from thousands of people like you, and creating large blocks of funds that are in the millions of dollars. This gives the Trust a leverage position whereby we can command large profits, and have the security of never putting the principal at risk. This is very sophisticated investing that cannot be accomplished unless you have millions of dollars to deposit in a top world U.S. bank.

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151. Inasmuch as we conclude that horizontal commonality exists here, we need not now decide if we should also adopt a vertical commonality analysis.

App. 261a. However, TIGC argues that commonality is nevertheless lacking because the investors did not "share proportionately in the profits or losses of TIGC or the various investment programs," Appellant's Br. at 19 (emphasis omitted). Rather, TIGC asserts that "each participant would execute an individual contract with TIGC providing for a fixed return, payable on demand (principal only) or on a specific date. . . . " *Id.* According to TIGC:

> [T]he property transfers were obligations of TIGC to repay the other party to the contract at a specific time, and did not represent a direct interest in TIGC, any other entity or a specific security or investment vehicle. . . . The property transfers were not earmarked for any particular purpose, or even any particular type of investment. . . . Under these contracts, the TIGC Board retained exclusive control over the investment decision and participants were not promised that their funds would be invested in any particular investment program.

Id. at 18 (internal citations omitted).

However, TIGC's denial of horizontal commonality is contrary to the record. By the plan's very terms, the return on investment was to be apportioned according to the amounts committed by the investor. Each investor's apportionment of profits was represented by certain "capital units" obtained in exchange for executing a "property transfer agreement." The number of units an investor purchased was, of course, dependent upon the size of his or her investment and the investor's return was directly proportional to the amount of that investment. TIGC's solicitation materials stated:

> [W]ith the Private Trust, what you will be doing is making a Property Transfer into the Trust in exchange for 1 Capital Unit for every $100 deposit. In turn the Trust guarantees that you will make a certain annual dividend. These dividends are a minimum of 20% up to 181% depending on the amount of Capital Units you hold.

Supp. App. 77. The materials also stated that "[d]ividends are dispersed . . . as the assets of the Trust increase and as the Board of Trustees elects to pay guaranteed dividends," App. 261a.

TIGC seeks to negate the obvious import of its structure by arguing that there are technical characteristics that distinguish the instruments involved here from those that are "securities." We are not persuaded. The defendants' claim that the property transfer contracts do not constitute "investment contracts" because the investors were to receive a fixed rate of return rather than a rate dependent on the success of the investments. The defendants argue:

> [I]f the aggregate value of the investments increased, each contract holder would not share in the appreciation. Rather, they would receive only their fixed, contractually agreed-upon return. . . . Similarly, if the value of TIGC investments decreased, the contract holder would still be entitled to the agreed-upon, fixed return on his or her property transfer contract. . . . In the event that the value of the investments dropped below the ability of TIGC to honor its commitment to a specific individual, the participants would not share proportionately ('pro rata') in the shortfall.

Appellant's Br. at 19 (internal citations omitted). However, the definition of security does not turn on whether the investor receives a variable or fixed rate of return. *See El Khadem v. Equity Securities Corp.*, 494 F.2d 1224, 1229 (9th Cir. 1974) (that expected profits remain constant while risk of loss varies does not remove a plan from the definition of a security); *National Bank of Yugoslavia v. Drexel Burnham Lambert, Inc.*, 768 F.Supp. 1010, 1016 (S.D.N.Y. 1991) (holding that time deposits made for investment purposes in return for a fixed rate of interest were investment instruments rather than consumer or commercial bank loans).

Profits can be either "capital appreciation resulting from the development of the initial investment" or earnings contingent on profits gained from the use of investors' funds. *United Housing Foundation, Inc. v. Forman*, 421 U.S. 837, 852 (1975). The mere fact that the expected rate of return is not speculative does not, by itself, establish that the property transfer contracts here are not "investment contracts" within the meaning of federal securities laws. *See Howey*, 328 U.S. at 301 (explicitly rejecting the theory that a non-speculative enterprise cannot be considered an investment contract; "it is immaterial whether the enterprise is speculative or non-speculative").

Moreover, the transactions here are easily distinguished from those in *Marine Bank v. Weaver*, 455 U.S. 551 (1982), where the Supreme Court held that FDIC-protected certificates of deposit offering a fixed rate of return were not securities. There, the Supreme Court stated that Congress "did not intend to provide a broad federal remedy for all fraud." *Id.* at 557. The Court reasoned that

certificates of deposit issued by federally-regulated banking institutions differed from other long-term debt obligations in part because "[i]t is unnecessary to subject issuers of bank certificates of deposit to liability under the antifraud provisions of the federal securities laws since the holders of bank certificates of deposit are abundantly protected under federal banking laws," *Id.* at 559. The Court noted that a "purchaser of a certificate of deposit is virtually guaranteed payment in full," *Id.* at 551. Here, TIGC's investors were offered no such protection.[9] "The crux of the *Marine Bank* decision is that federal banking regulations and federal deposit insurance eliminate the risk of loss to the investor, therefore obviating the need for protection of the federal securities laws," *Gary Plastic Packing Corp. v. Merrill Lynch*, 756 F.2d 230, 240 (2d Cir. 1985).[10] As will become more evident in our discussion of TIGC's "investment" in certain railroad bonds, the investors here were guaranteed nothing despite TIGC's purported guarantee of principal. "The fundamental purpose undergirding the Securities Acts is

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[9] TIGC's investors are therefore like "the holder[s] of an ordinary long-term debt obligation (who) assume[ ] the risk of the borrower's insolvency." *Id.* at 551-52.

[10] Defendants contend that "just because the property transfers at issue in this case do not constitute securities does not mean they were exempt from any form of regulation whatsoever. Perhaps there are other branches of government, state or federal, with jurisdiction over TIGC, or other regulations or statutes which TIGC's conduct violated." Appellant's Br. at 20. However, they do not identify any applicable regulation or statute. This is consistent with our conclusion that this enterprise required the protections of federal securities laws.

'to eliminate serious abuses in a largely unregulated securities market,' " *Reves v. Ernst & Young*, 494 U.S. 56, 60 (1990) (*quoting United Housing*, 421 U.S. at 849 (*distinguishing Marine Bank* where no risk-reducing factor was present)).

> The aim is to prevent further exploitation of the public by the sale of unsound, fraudulent, and worthless securities through misrepresentation; to place adequate and true information before the investor; to protect honest enterprise, seeking capital by honest presentation, against the competition afforded by dishonest securities offered to the public through crooked promotion. . . .

S.Rep. No. 47, 73d Cong., 1st Sess., at 1 (1933).

We take a flexible and realistic approach in determining when a particular scheme requires the protection of federal securities laws.

For example, in *Howey*, the defendant owned large tracts of citrus acreage that it sold to the public. Purchasers of the tracts received land sales and service contracts and, upon full payment of the purchase price, the land was conveyed by warranty deed. However, under the arrangement between Howey and the purchasers, a servicing corporation was given "full and complete" possession of the acreage, and full discretion to grow, harvest, and market crops grown on the tracts with very little accountability to the purchaser. The SEC instituted an action against Howey because the corporation had not complied with the registration requirements of federal

securities laws. Howey defended by arguing that registration was not required because it was not selling "securities" under federal law. The "lower courts . . . treated the contracts and deeds as separate transactions involving no more than an ordinary real estate sale and an agreement by the seller to manage the property for the buyer," *Howey*, 328 U.S. at 297-98, and concluded that they did not constitute "securities" under federal law. However, the Supreme Court disagreed because Howey was not merely offering fee simple interests in land coupled with a contract for management services. Rather, the Court concluded that Howey was offering "an opportunity to contribute money and to share in the profits" of the enterprise. *Id.* at 299. "[The purchasers were] attracted solely by the prospects of a return on their investment," and the land sales contracts and warranty deeds were merely a "convenient method" by which to apportion profits. *Id.* at 300. Thus, the Court concluded that the agreements were securities. The Court reasoned:

> The investors provide the capital and share in the earnings and profits; the promoters manage, control and operate the enterprise. It follows that the arrangements whereby the investors' interests are made manifest involve investment contracts, *regardless of the legal terminology in which such contracts are clothed.*

Id. (emphasis added). *See also SEC v. C.M. Joiner Leasing Corp.*, 320 U.S. 344 (1943) (finding that a defendant selling assignment of oil leases was "not as a practical matter offering naked leasehold rights," instead "the (oil) exploration enterprise was woven into these leaseholds, in both an economic and a legal sense; the undertaking to

drill a well runs through the whole transaction as the thread on which everybody's beads were strung.")

Here, the investors' beads were strung upon the gossamer guarantee of seemingly impossibly high returns at no risk. The fact that TIGC promised a "fixed rate of return" based upon the amount invested is irrelevant. We will not embroider a loophole into the fabric of the securities laws by limiting the definition of "securities" in a manner that unduly circumscribes the protection Congress intended to extend to investors. Rather, we must scrutinize these "property transfer contracts" in a manner that "permits the fulfillment of the statutory purpose of compelling full and fair disclosure relative to the issuance of the many types of instruments that in our commercial world fall within the ordinary concept of a security." *Howey*, 328 U.S. at 299 (internal quotation marks and citation omitted). Our inquiry:

> embodies a flexible rather than a static principle, one that is capable of adaptation to meet the countless and variable schemes devised by those who seek the use of the money of others on the promise of profits.

Id.

We must consider that Congress "enacted a definition of 'security' sufficiently broad to encompass virtually any instrument that might be sold as an investment," *Reves*, 494 U.S. at 61. The securities laws were intended to provide investors with accurate information and to protect the investing public from the sale of worthless securities through misrepresentations. H.R.Rep. No. 85, 73d Cong., 1st Sess., at 1-5 (1933). As noted above, TIGC accepted nearly $26.6 million from approximately 10,000

investors. TIGC persuaded those investors to part with their cash by guaranteeing the proverbial "blue sky;" fantastic profit at no risk. Of the $26.6 million raised, more than half of the money was used to satisfy the material "needs" of the individual defendants. The balance was poured down empty wells that could hardly be confused with prudent investments. TIGC *realized no return whatsoever* on those "investments." Given the totality of the circumstances here, the property transfer contracts clearly constitute securities, and the district court therefore had subject matter jurisdiction.

IV.

Defendants argue that the SEC failed to establish the scienter required for liability under Section 17(a) of the Securities Act,[11] Section 10(b) of the Exchange Act[12] or Rule 10b-5.[13] They argue that they cannot therefore be

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[11] Section 17(a) makes it unlawful for any person in the offer or sale of any security to: (1) "employ any device, scheme or artifice to defraud;" (2) "obtain money or property by means of any untrue statement [or omission] of material fact;" or (3) to "engage in any transaction, practice or course of business which operates . . . as a fraud or deceit upon the purchaser." 15 U.S.C. § 77q(a).

[12] Section 10(b) of the Exchange Act prohibits "manipulative" or "deceptive" conduct "in connection with the purchase or sale of a security." 15 U.S.C. § 78j(b).

[13] Rule 10b-5 proscribes (1) the employment of any "device, scheme or artifice to defraud;" (2) the making of "any untrue statement [or omission] of material fact;" and (3) the engagement "in any act, practice, or course of business which operates . . . as a fraud or deceit upon any person, in connection with the purchase or sale of any security." 17 C.F.R. § 240.10b-5.

liable even if the property transfer contracts were securities.

The SEC must establish the requisite scienter to establish securities fraud. *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 193 (1976); *Newton v. Merrill, Lynch, Pierce, Fenner & Smith, Inc.*, 135 F.3d 266, 272-73 (1998); *McLean v. Alexander*, 599 F.2d 1190, 1196-97 (3d Cir. 1979). Scienter is "a mental state embracing intent to deceive, manipulate or defraud," *Hochfelder*, 425 U.S. at 193 n.12; *McLean*, 599 F.2d at 1197. We have previously held that the scienter required for securities fraud includes recklessness, and we have adopted the definition of recklessness set forth in *Sundstrand Corp. v. Sun Chemical Corp.*, 553 F.2d 1033 (7th Cir. 1977). *See also Sharp v. Coopers & Lybrand*, 649 F.2d 175, 193 (3d Cir. 1981).[14] Accordingly, recklessness includes:

> [H]ighly unreasonable (conduct), involving not merely simple, or even inexcusable negligence, but an extreme departure from the standards of ordinary care, . . . which presents a danger of misleading buyers or sellers that is either known to the defendant or is so obvious that the actor must have been aware of it.

McLean, 599 F.2d at 1197 (*citing Sundstrand Corp.*, 553 F.2d at 1045).

The SEC argues that scienter is evidenced by TIGC's guarantees of high rates of return that were unsupported by any honest due diligence. The defendants, on the other hand, contend that their actions "were entirely consistent

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[14] The recklessness standard applies to both omissions and misstatements. *McLean*, 599 F.2d at 1197.

with the fact that they believed their representations (in the Trust literature and elsewhere) [to be] true." Appellant's Br. at 23. However, good faith, without more, does not necessarily preclude a finding of recklessness. Therefore, even if the defendants believed TIGC's investments were sound, they may still be liable for securities fraud if their belief was based upon nothing more than a reckless disregard of the truth. Moreover, we reiterate that TIGC invested less than half of the money obtained under the property transfer contracts. In addition, a minimum of $3,649,000 of the funds was spent on such things as the Bensons' home, a new Mercedes Benz, etc. Nevertheless, the defendants claim that they "attempted to obtain documentation and contractual guarantees from the investment providers" and "were [themselves] the victims of fraud on the part of the investment providers." *Id.* at 29-30. We are not persuaded.

The defendants concede that no profits were ever realized from the funds that were actually invested. Appellant's Br. at 11. One need look no further than one example of an investment that TIGC made to understand why no profit was ever realized and to appreciate the specious nature of the denials of recklessness. In October 1996, TIGC purchased a bond of the Marietta and Northern Georgia Railway that had been issued in 1889. TIGC paid $302,000 for that bond, apparently based upon "unsubstantiated boasts of value ranging from $35 million to $107 million, and without performing any meaningful type of due diligence inquiry to clarify the $72 million discrepancy." Appellee's Br. at 28. TIGC paid $302,000 even though the bond had a face value of only $1000. Despite the unique investment acuity proclaimed

in the Trusts' materials, the defendants missed a little glitch in this investment bonanza. The railroad that issued the bond had gone bankrupt in 1895, and it had ceased to exist in 1896. Supp. App. 1-4. The bond was therefore "worthless except for its modest value as a collectible (which [was] estimated at $80-100.)." Appellee's Br. at 29. Thus, TIGC used a portion of those funds that it did not divert to personal use to pay $302,000 for a bond with a face value of $1,000 that had been issued by a railroad that had gone out of business 100 years ago.[15] In referring to this investment the district court stated:

> [W]e suspect that even a complete neophyte in finance, accounting, or economics would suspect, when confronted with such an investment, that defendants' business was on the wrong track. Instead, TIGC chose in its materials to value the ancient bond at $107 million!

993 F.Supp. at 330. It is a small wonder that the district court referred to TIGC as a "financial train wreck." *Id.* at 326. Yet, TIGC's offering materials proclaimed that the unique skill it provided would enable the Trust to guarantee very high rates of return with no risk to principal. The solicitation materials boasted that participants would have "an opportunity that has a 100% success rate, for 100% of the people who become associated with my business." Supp.App. 74. Investors were told that their investments were "guaranteed by a top 100 World Bank" and "the returns (Profits) that (TIGC based) the [return rate of] 138% and 181% on (were) guaranteed by the

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[15] This investment was therefore the ultimate "turn around play."

Trust, making this one of the safest programs available." App. 271a (emphasis omitted).

Even if we indulge the defendants and assume *arguendo* that they believed in these guarantees, we nevertheless must examine the foundation such a belief would have rested upon. A good faith belief is not a "get out of jail free card." It will not insulate the defendants from liability if it is the result of reckless conduct. *See McLean*.[16] However, under our standard of review, we must view the evidence in the light most favorable to the SEC as verdict winner. *Eisenberg v. Gagnon*, 766 F.2d 770, 778 (3d Cir. 1985). In doing so, we readily conclude that the district court did not err in finding that the SEC had established the necessary scienter for securities fraud. The district court stated:

> [W]e reject Geoffrey Benson's proffered defense that he was ignorant of the falsity of TIGC's statements, and in all events he acted in good faith in soliciting investor funds and pursuing investments on behalf of TIGC. Even assuming that those statements are true – and we do not, given the mountain of evidence of invidious motive here – ignorance provides no defense to recklessness where a reasonable investigation would have revealed the truth to the defendant. . . . Similarly, good faith is no shield to liability under the antifraud provisions of the Securities Acts. . . .

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[16] We will *assume* that a defendant can genuinely have a subjective belief that demonstrates good faith even though it is the result of reckless conduct. However, it clearly can be argued that a subjective belief based only upon an inquiry that is reckless can never properly be considered a "good faith" belief.

But we need not rely on either the ignorance defense, or the existence of recklessness, in Geoffrey Benson's case. His actual intent to defraud may be inferred from his wholly successful, and carefully-crafted, offering materials. . . . [T]he materials at length depict a mysterious cabal into which only the initiated, like TIGC's trustees, could enter. Benson's texts weave visions of risk-free, high-return investing in a clever tapestry of anti-government, individualist fervor. Although the offering materials often speak of mysteries and the need to maintain secrecy, in fact Geoffrey Benson and his colleagues well knew that the reason these secrets were not mentioned is because there were none. As Geoffrey Benson and O'Connor allowed their offering materials to be disseminated around the country – by fax on demand, through a legion of downline representatives, and via the mails – they had to know that they were funding payments to early investors with new investors' money rather than with investment return. In short, Geoffrey Benson and Geoffrey O'Connor knew precisely what they were doing in these materials, and that was engaging in a hugely successful interstate fraud.

At best, defendants' investment enterprise began as a reckless financial enterprise, and evolved into an intentional scheme to defraud investors of their money when that money became necessary to prevent TIGC's collapse. At worst, TIGC's Asset Enhancement Program was from its inception a Ponzi scheme, calculated to bilk investors of funds by preying on their excessive greed, their feelings of exclusion from America's current prosperity, and their fears of jackbooted government intrusion.

993 F. Supp. at 330-31.[17] The district court's analysis is consistent with the record. Indeed, the record mandates the court's conclusion.

In *McLean*, we stressed that plaintiff:

> [c]ircumstantial evidence may often be the principal, if not the only, means of proving bad faith. A showing of shoddy accounting practices amounted at best to a 'pretended audit,' or of grounds supporting a representation 'so flimsy as to lead to the conclusion that there was no genuine belief back of it' have traditionally supported a finding of liability in the face of repeated assertions of good faith. . . . In such cases, the factfinder may justifiably conclude that despite those assertions the 'danger of misleading . . . ' (was) so obvious that the actor must have been aware of it.

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[17] TIGC's materials also offered not so subtle hints that TIGC could assist in "sheltering" assets where others with less expertise had failed. TIGC's materials proclaimed:

> If you are thinking about establishing an off-shore Trust or Bank Account please beware! Belize, the Cayman's and may *[sic]* others that used to be off-shore havens are about as safe as throwing your money in the fireplace. The U.S. government has twisted most of these off-shore government's arms to the point where they will give out information and let the U.S. do whatever they want to.
>
> We have access to off-shore facilities that are totally safe when set up properly. If you are serious, and do not mind spending some time and money, you will want to contact us to get some of the preliminary details.

Supp. App. 88-89.

McLean, 599 F.2d at 1198 (*citing Sundstrand*, 553 F.2d at 1045) (footnotes omitted)). Although defendants assert a good faith belief that their representations were true, "an opinion that has been issued without a genuine belief *or reasonable basis* is an 'untrue' statement which, if made knowingly or recklessly, is culpable conduct actionable under [the securities laws]." *Eisenberg*, 766 F.2d at 776 (emphasis added).

> When the opinion or forecast is based on underlying materials which on their face or under the circumstances suggest that they cannot be relied on without further inquiry, then the failure to investigate further may 'support [ ]an inference that when [the defendant] expressed the opinion it had no genuine belief that it had the information on which it could predicate that opinion.'

Id. (*citing McLean*, 599 F.2d at 1198). Here, the evidence supporting TIGC's purported belief in its representations is "so flimsy as to lead to the conclusion that there was no genuine belief" in the validity of TIGC's guarantee or the soundness of its investments. *McLean*, 599 F.2d at 1198 (*citing Ultramares Corp. v. Touche*, 174 N.E. 441 (N.Y. 1931)). The guarantees were "so recklessly made that the culpability attaching to such reckless conduct closely approaches that which attaches to conscious deception," *Id.* at 1197 (*citing Coleco Industries, Inc. v. Berman*, 567 F.2d 569, 574 (3d Cir. 1977)). Indeed, here, the recklessness can be equated to conscious deception, especially when we consider how the defendants' primary focus was upon improving their own (apparently lavish) lifestyle rather than attempting to get a decent (let alone extraordinary) rate of return on the investments of the participants in the Trust.

The Trust failed: (1) to obtain certified financial statements from the programs in which it invested, (2) to inquire into whether programs were insured or guaranteed by a banking institution, (3) to obtain legal opinions about the legitimacy of the investment programs and (4) to obtain certificates of good standing.[18]

We are equally unpersuaded by the defendants' attempts to shift the responsibility to the purported "dishonest and fraudulent activities" of the investment providers. Appellant's Br. at 28. Although several of the investment companies that TIGC did business with are now either defunct or under investigation, the evidence is inconsistent with TIGC as a mere "victim." Rather, it appears that several scoundrels were sleeping in the same bed, and these defendants were amongst them. We doubt that it was a mere oversight that TIGC continued to guarantee high rates of return even after defaults in $7.5 million worth of their investments. Thus, even if the initial guarantees were not recklessly made, the record would still support a finding that TIGC was reckless in failing to modify its guarantees after such massive

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[18] We also note that TIGC's "warning of risk" was less than forthcoming. For example, the solicitation materials stated:

> Yes we do guarantee the returns you will make on your exempt security transfer. . . . (P)lease do not interpret guarantee as meaning absolutely no risk. There is no such thing. There's a risk in getting out of bed in the morning. Or . . . a big rock could fall on Ohio and wipe out TIGC and everything else in the state. Remember, things can happen that are beyond anyone's control.

App. 230a.

defaults. Accordingly, we hold that the SEC presented abundant evidence of the scienter requirement of securities fraud. *See McLean*, 599 F.2d at 1197.

V.

Defendants next contend that the district court erred in denying their concededly untimely demand for a jury trial. The SEC filed its Complaint on August 27, 1997. The defendants filed an Answer on September 26, 1997; and relief defendants filed an Answer on October 28, 1997. The defendants did not file their Demand for Jury Trial until January 13, 1998; two and one half months after the final pleading in this case.

Fed. R. Civ. P. 38 states, in pertinent part, "Any party may demand a trial by jury of any issue triable of right by a jury by . . . serving upon the other parties a demand thereof in writing at any time after the commencement of the action and not later than 10 days after the service of the last pleading directed to such issue . . . ," Fed.R.Civ.P. 38(b). Fed R. Civ. P. 39(b) provides, "[N]otwithstanding the failure of a party to demand a jury in an action in which such a demand might have been made of right, the court in its discretion upon motion may order a trial by jury of any or all issues." Fed.R.Civ.P. 39(b). Therefore, a district court may still grant a jury trial, even where the demand was untimely made.

We review the district court's denial of the request for a jury trial for abuse of discretion. *William Goldman Theatres v. Kirkpatrick*, 154 F.2d 66, 68 (3d Cir. 1946). "An abuse of discretion is a 'clear error of judgment,' and not simply a different result which can arguably be obtained

when applying the law to the facts of the case." *In re Tutu Wells Contamination Litigation*, 120 F.3d 368, 387 (3d Cir. 1997) (*quoting United Telegraph Workers, AFL-CIO v. Western Union Corp.*, 771 F.2d 699, 703 (3d Cir. 1985)). Although we understand that the delay here may have been partly attributable to a change in counsel, it is nevertheless uncontested that the only justification for the delay was attorney inadvertence. Courts in this Circuit generally deny relief when "the only basis for such relief advanced by the requesting party is the inadvertence or oversight of counsel." *See Plummer v. General Elec. Co.*, 93 F.R.D. 311, 313 (E.D. Pa. 1981); and cases cited therein. However, this is not a mechanical rule.

Courts consider several factors in determining whether to grant an untimely jury demand. They are:

> 1) whether the issues are suitable for a jury; 2) whether granting the motion would disrupt the schedule of the Court or the adverse party; 3) whether any prejudice would result to the adverse party; 4) how long the party delayed in bringing the motion; and 5) the reasons for the failure to file a timely demand.

Fort Washington Resources, Inc. v. Tannen, 852 F. Supp. 341, 342 (E.D. Pa. 1994). Here, in denying the untimely request, the district court noted that (i) "Defendants offer nothing to excuse their untimeliness except the fact that they switched counsel in mid-November" – a full two months prior to making the demand, and (ii) "the fact that the demand was made only two weeks before trial – and not fully briefed until one week before trial – means that the Commission's case would be greatly prejudiced by our granting the motion." App. 118a. The district court

did not abuse its discretion in denying the belated request for a jury trial under these circumstances.

We agree that the defendants did not make an adequate showing that the issues involved in this case were particularly suitable for a jury. Contrary to the defendants' assertion, we have rejected an argument for entitlement to a jury trial based upon the quantum of damages. *William Goldman Theatres*, 154 F.2d at 69 ("evidentiary facts are intricate and will require auditing, if not an accounting[,][w]e can perceive substantial difficulties, though not insuperable obstacles, to the framing of a charge which properly would submit the issue of damages to a jury").

The defendants also argue that the scheduling of the initial preliminary injunction hearing created time pressures resulting in counsel's failure to timely file a jury demand. Specifically, they argue that after new counsel entered their appearance in mid-November, "they faced the time consuming task of absorbing and assessing the facts, the procedural posture of the case, and potential trial strategies," as well as conducting discovery. Appellant's Br. at 32-33. The district court concluded that defendants' explanations "(fell) short" of excusing their untimely demand. App. 118a-19a. We agree.

We disagree, however, with the district court's conclusion that granting the belated jury request would have materially prejudiced the SEC under the circumstances here. Nevertheless, based upon all of the factors we have enumerated, we hold that the district court did not abuse its discretion in denying defendants' untimely demand for a jury trial.

VI.

The defendants contend that the cumulative effect of four alleged evidentiary and procedural errors impaired their right to present and prepare an adequate defense. This aggregation of errors is known as the "cumulative error doctrine." Under that doctrine appellate courts may determine that, although certain errors do not require relief when considered individually, the cumulative impact of such errors may warrant a new trial. In other words, under this theory, the whole is greater than the sum of its parts. However, unlike some of our sister courts of appeals,[19] we have rejected the cumulative error doctrine, at least in the context of a civil trial. *See Lockhart v. Westinghouse Credit Corporation*, 879 F.2d 43, 57 (3d Cir. 1989), *overruled on other grounds by Starceski v. Westinghouse Elec. Corp.*, 54 F.3d 1089 (3d Cir. 1995). Moreover, even if we were to apply the doctrine of cumulative error, we would conclude that defendants are entitled to no relief because the individual rulings that they challenge under that doctrine were not erroneous.

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[19] *See e.g., United States v. Rivera*, 900 F.2d 1462, 1469 (10th Cir. 1990) ("The cumulative effect of two or more individually harmless errors has the potential to prejudice a defendant to the same extent as a single reversible error"); *Malek v. Federal Ins. Co.*, 994 F.2d 49, 55 (2d Cir. 1993); *Frymire-Brinati v. KPMG Peat Marwick*, 2 F.3d 183, 188 (7th Cir. 1993); *Hendler v. United States*, 952 F.2d 1364, 1383 (Fed. Cir. 1991).

A.

Defendants claim that the district court erred in "cutting . . . fees for defense counsel" two days before the final injunction hearing and thereby "unfairly (hampering) the defense efforts to complete discovery and to mount an effective defense at trial." Appellant's Br. at 35. In November 1997, the district court issued a preliminary injunction authorizing a court-appointed trustee to disburse $125,000 for legal fees and expenses on behalf of the defendants from the previously frozen assets. As a result of receiving information that the defendants were independently attempting to raise $175,000 to defray legal expenses, the SEC successfully moved to modify the district court's original provision of legal fees and expenses. Two days before the final injunction hearing began, the district court granted the SEC's motion in part, and issued an order prohibiting defense counsel from disposing of further trust assets to raise funds for fees or expenses.

The authority to freeze assets in receivership, in whole or in part, is committed to the district court's sound discretion. *Commodity Futures Trading Commission v. American Metals Exchange Corp.*, 991 F.2d 71, 79 (1993). A freeze of assets is designed to preserve the status quo by preventing the dissipation and diversion of assets. *Id.* (*quoting SEC v. Capital Counsellors, Inc.*, 512 F.2d 654 (2d Cir. 1975)). Here, the district court's order modifying the initial release of legal expenses and fees was prudent inasmuch as the defendants were attempting to raise

funds to pay for legal services.[20] In *American Metals*, we found no abuse of discretion where the district court denied a request to pay attorney's fees from frozen assets where it was shown that the defendant had access to other funds not in receivership. Accordingly, we do not find abuse of discretion here.

B.

Defendants argue that the district court erred in "arbitrarily advancing the date for the (final injunction hearing) by two days" because defense was operating

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[20] The record indicates that Infinity investors received the following correspondence from the "Freedom For America Ministry and Friends of Infinity":

> The SEC, government, the Judge, or Trustee (It's hard to tell any of them apart) has approved an 'allowance' out of YOUR 'MONEY' to be paid to us to live on. . . . Each and everyone of you can help with your gift to FAM, along with the completed form provided. Your gift at this time is important because the government has frozen [NOT SEIZED] all assets of TIGC and related entities which makes it impossible at this time for them to fund a Member Law Suit against the government, or to adequately finance their own offense. Your gift will be used for the following: Administrative and operating . . . expenses . . . 15%, Private Member Law Suit . . . 25%, legal offense fund for TIGC . . . 25%, and investments . . . 35%. If the average gift is $100.00, FAM would have about $175,000 to fund a TIGC Member Suit, $175,000 to help TIGC with their legal costs, and $245,000 for investment purposes over a period of time.

Supp. App. 145-46.

under an expedited discovery schedule and "could not afford to lose the two full days in which to prepare" for the final injunction hearing. Appellant's Br. at 35. This claim is wholly without merit.

Matters of docket control and scheduling are within the sound discretion of the district court. *State of Alaska v. Boise Cascade Corp.*, 685 F.2d 810, 817 (3d Cir. 1982). Here, the district court notified both parties, over three weeks before the originally scheduled date, that the hearing date would have to be changed due to changes in the district court's criminal docket. We find neither "actual" nor "substantial" prejudice in the rescheduling. The change was only two days, and it impacted both sides.

C.

Defendants allege error in the court's refusal to admit lay opinion testimony from John F. Jackman, an insurance specialist whom defendants called to testimony about "legitimate bank instruments and other investment programs which produce extremely high returns with minimal risk." Appellant's Br. at 36. The defendants contend that Mr. Jackman's testimony "was probative of the issue of whether [TIGC was] reckless or acted with an intent to defraud" and would contradict the finding that the promised rates of return were unlikely. *Id.* at 37. We review the exclusion of lay opinion testimony for abuse of discretion. *Government of the Virgin Islands v. Knight*, 989 F.2d 619, 629 (3d Cir. 1993). Rule 701 of the Federal Rules of Evidence provides:

> If the witness is not testifying as an expert, the witness' testimony in the form of opinion or

> inferences is limited to those opinions or inferences which are (a) rationally based on the perception of the witness and (b) helpful to a clear understanding if the witness' testimony or the determination of a fact in issue.

Fed. R. Evid. 701. A lay opinion is rationally based on the witness' perception and "firsthand knowledge of the factual predicates that form the basis for the opinion." *Knight*, 989 F.2d at 629 (*citing* Fed. R. Evid. 701(a) advisory committee's note). Here, it is uncontested that Jackman had no personal knowledge of the investments in question. Therefore, the court properly barred his testimony. Moreover, even though defendants now seize upon Jackman's precluded testimony to support their cries of "foul," it is obvious that excluding his testimony did them far more good than admitting his questionably relevant opinion would have. In his deposition, Jackman testified that it was not possible to guarantee the high rates of return promised by TIGC. Supp. App. 153-154. When he was asked how he would respond to someone who offered the sky-high returns and guarantee of principal promised by TIGC he responded: "I'd say you were nuts, and your [you're] inexperienced, and you don't know what you're talking about, and you're a fool." *Id.* at 156. It is hard to see how the defendants were prejudiced by excluding such testimony.

D.

Finally, the defendants contend that the district court erred in excluding certain "key exhibits" that they failed to list in the pretrial statement. Defendants assert that the admission of the documents would have "demonstrated

that the Defendants acted in good faith, with no intent to defraud and had exercised some care in making investments." Appellant's Br. at 35.

We review a district court's decision to refuse to admit exhibits not previously identified for abuse of discretion. *Greate* [sic] *Bay Hotel & Casino v. Tose*, 34 F.3d 1227, 1236 (3d Cir. 1994). In determining whether there has been an abuse of discretion, we consider four factors: (1) the prejudice or surprise in fact to the opposing party, (2) the ability of the party to cure the prejudice, (3) the extent of disruption of the orderly and efficient trial of the case, and (4) the bad faith or willfulness of the noncompliance. *Id.* (*quoting Beissel v. Pittsburgh and Lake Erie R. Co.*, 801 F.2d 143, 150 (3d Cir. 1986)). Here, the district court only excluded those documents that the defendants failed to produce, App. 144a-45a, and the district court properly considered the effect that admitting the evidence would have on the SEC. The court stated, "The Commission is entitled not to be surprised. That's why we have all these procedures in Federal Court." Supp. App. 59. We find no abuse of discretion in that.

VII.

Accordingly, for the reasons set forth above, we will affirm the district court's Order for Final Injunction.

A True Copy:
Teste:

Clerk of the United States Court of Appeals for the Third Circuit

UNITED STATES COURT OF APPEALS
FOR THE THIRD CIRCUIT

Nos. 98-1215, 98-1216, 98-1217

UNITED STATES SECURITIES AND
EXCHANGE COMMISSION

v.

THE INFINITY GROUP COMPANY; GEOFFREY P. BENSON; GEOFFREY J. O'CONNOR; FUTURES HOLDING COMPANY; SLB CHARITABLE TRUST; SUSAN L. BENSON; JGS TRUST; LINDSAY SPRINGER; BONDAGE BREAKER MINISTRIES

LINDSAY SPRINGER; BONDAGE
BREAKER MINISTRIES,

THIRD-PARTY PLAINTIFFS

v.

THE UNION STATES OF THE CONSTITUTION, i.e.; ALASKA; ALABAMA; ARKANSAS; ARIZONA; CALIFORNIA; COLORADO; CONNECTICUT; DELAWARE; FLORIDA; GEORGIA; HAWAII; IOWA; ILLINOIS; INDIANA; KANSAS; KENTUCKY; LOUISIANA; MASSACHUSETTS; MARYLAND; MAINE; MICHIGAN; MINNESOTA; MISSOURI; MISSISSIPPI; MONTANA; NORTH CAROLINA; NORTH DAKOTA; NEBRASKA; NEW HAMPSHIRE; NEW JERSEY; NEW MEXICO; NEVADA; NEW YORK; OHIO; OKLAHOMA; OREGON; PENNSYLVANIA; RHODE ISLAND; SOUTH CAROLINA; SOUTH DAKOTA; TENNESSEE; TEXAS; UTAH; VIRGINIA; VERMONT; WISCONSIN; WEST VIRGINIA;

WYOMING; WASHINGTON; FEDERAL STATE DISTRICT OF COLUMBIA,

THIRD-PARTY DEFENDANTS

Geoffrey J. O'Connor (98-1215), Geoffrey P. Benson (98-1216), Susan L. Benson, Pro Se on behalf of herself and in her representative capacity on behalf of SLB Charitable Trust, Futures Holding Company and JGS Trust (98-1217)

Appellants

Present: Alito, McKee, *Circuit Judges*, and Schwartz, *District Judge**

JUDGMENT

These causes came on to be heard on the record from the United States District Court for the Eastern District of Pennsylvania and were argued by counsel on March 2, 1999.

On consideration whereof, it is now here ordered and adjudged by this Court that the judgment of the said District Court entered February 9, 1998, be, and the same is hereby affirmed. Costs taxed against appellants. All of the above in accordance with the opinion of this Court.

ATTEST:
/s/ Maria M. Waldron
Acting Clerk

Dated: 4 May, 2000

*The Honorable Murray M. Schwartz, Senior District Judge of the United States District Court for the District of Delaware, sitting by designation.

IN THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF PENNSYLVANIA

SECURITIES AND EXCHANGE COMMISSION	:	CIVIL ACTION
v.	:	
THE INFINITY GROUP COMPANY, et al.	:	NO. 97-5458

MEMORANDUM

Dalzell, J. February 5, 1998

Now before us is an action the Securities and Exchange Commission (hereinafter "SEC" or "Commission") filed on August 27, 1997, alleging that defendants Geoffrey P. Benson, Geoffrey J. O'Connor, and The Infinity Group Company (hereinafter "TIGC") engaged in an ongoing scheme to defraud public investors of their money through the offer and sale of TIGC securities. The complaint further charged that the defendants' actions violated Section 20(b) of the Securities Act of 1933, 15 U.S.C. § 77t(b) (hereinafter "1933 Act"), and Section 21(d) of the Securities Exchange Act of 1934, 15 U.S.C. 78u(d) (hereinafter "1934 Act"). The Commission sought an injunction barring defendants from violating the two Acts, and disgorgement of ill-gotten gains. In addition, the SEC also sought disgorgement from relief defendants Susan L. Benson, JGS Trust, SLB Charitable Trust, Futures Holding Company, and Lindsey K. Springer d/b/a Bondage Breaker Ministries.

On the same day the SEC filed the complaint, Judge Brody, as Emergency Judge, granted the Commission's

motion for a temporary restraining order, temporarily enjoining defendants from future violations of the federal securities laws and freezing defendants' and relief defendants' assets.

After hearings on September 3 and 4, 1997, on September 5, 1997, we granted the Commission's motion for a preliminary injunction in the matter. In addition to continuing the injunction and asset-freeze granted in the TRO we also, *inter alia*, appointed Robert F. Sanville, C.P.A., as trustee of the TIGC Trust. We empowered Mr. Sanville to take control and possession of all of TIGC's funds, assets, and other property of TIGC, and directed him to provide an accounting of the Trust. On January 16, 1998, the Trustee submitted that account.

We held a final injunction hearing on February 2 through 4, 1997, at the close of which defendants filed what they styled as a "motion" to dismiss under Fed. R. Civ. P. 12(b)(1), but which in reality is a suggestion of lack of subject matter jurisdiction under Fed. R. Civ. P. 12(h)(3). *See Berkshire Fashions, Inc. v. M.V. Hakusan II*, 954 F.2d 874, 880 n.3 (3d Cir. 1992) (noting that the distinction between the two "is simply that [a 12(h)(3) suggestion] may be asserted at any time and need not be responsive to any pleading of the other party"). Defendants' "motion" is without merit.

In order to invoke the protections of the securities laws, the Commission must, as a threshold matter, show that TIGC's "property transfer agreement" was a security. Among other categories of instruments included within the definition of a "security" under § 2(1) of the 1933 Act

and § 3(a)(10) of the 1934 Act is the category of "investment contracts." In *SEC v. W.J. Howey*, 328 U.S. 293, 66 S.Ct. 1100 (1946), the Supreme Court defined an investment contract as "a contract, transaction or scheme whereby a person invests his money in a common enterprise and is led to expect profits solely from the efforts of the promoter or a third party." *Id.* 66 S.Ct. at 1103. It is the representations made by the promoters, not their actual conduct, that determine whether an interest is an investment contract or other security. *SEC v. United Benefit Life Ins. Co.*, 387 U.S. 202, 211, 87 S.Ct. 1557, 1562 (1967); *SEC v. C.M. Joiner Leasing Corp.*, 320 U.S. 344, 351, 64 S.Ct. 120, 123-24 (1943).

There is ample documentary and testimonial evidence that many people invested money with TIGC. Indeed, the Trustee has produced a list of over 10,000 people, based on TIGC's own records, who invested in excess of $26.6 million in the TIGC Trust. Thus, element one of *Howey* is satisfied.

The Commission has also satisfied its burden of proof as to element two of *Howey*, which requires showing that, by mailing checks to TIGC, TIGC's members were investing in a "common enterprise." There are two definitions of a "common enterprise," one based on "horizontal commonality" and the other based on "vertical commonality." Horizontal commonality has been explicitly adopted by the our Court of Appeals, but that Court has not yet decided whether to adopt vertical commonality. *See Steinhardt Group, Inc. v. Citicorp*, 126 F.3d 144, 152 (3d Cir. 1997). We find that the record amply supports finding "horizontal commonality" in TIGC's operations, and therefore – although we think that vertical commonality

also exists on these facts, and we note that the Fourth, Eighth, Ninth, and Tenth Circuits have all adopted vertical as well as horizontal commonality[1] – we find it unnecessary to determine whether to adopt that definition as well.

According to our Court of Appeals, horizontal commonality "requires a pooling of investors' contributions and distribution of profits and losses on a pro-rata basis among investors." *Steinhardt*, 126 F.3d 144, 151 (3d Cir. 1997). *Salcer v. Merrill Lynch, Pierce, Fenner and Smith*, 682 F.2d 459, 469 (3d Cir. 1982), the only other Third Circuit case to address horizontal commonality, focused on pooling of investor funds. Our review of cases in other Circuits that apply the definition of horizontal commonality suggests that pooling of investor funds is most often the

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[1] The Fifth, Eighth, Ninth, and Tenth circuits have adopted "vertical commonality." *See Brodt v. Bache & Co., Inc.*, 595 F.2d 459, 461 (9th Cir. 1978); *SEC v. Koscot Interplanetary, Inc.*, 497 F.2d 473, 478 (5th Cir. 1974); *Miller v. Central Chinchilla Group, Inc.*, 494 F.2d 414, 418 (8th Cir. 1974); *McGill v. American Land & Exploration Co.*, 776 F.2d 923, 925 (10th Cir. 1985).

In an enterprise marked by vertical commonality, the investors' fortunes need not rise and fall together; a *pro rata* sharing of profits and losses is not required. Two distinct kinds of vertical commonality have been identified: "broad vertical commonality" and "strict vertical commonality". To establish "broad vertical commonality", the fortunes of the investors need be linked only to the efforts of the promoter. *See Revak v. SEC Realty Corp.*, 18 F.3d 81, 87 (2d Cir.1994). "Strict vertical commonality" requires that the fortunes of investors be tied to the fortunes of the promoter. *Id.* Here, there is clearly broad vertical commonality, and arguably strict vertical commonality as well.

determinative factor. It does not appear that the defendants object to the evidence of pooling, nor could they. TIGC's literature is rife with references to pooling, such as the following from a widely-distributed TIGC offering document:

> The Infinity Group Company invests for profit by accepting amounts as low as $1,200 from thousands of people like you, and **creating large blocks of funds that are in the millions of dollars.** This gives the Trust a leverage position whereby we can command large profits, and have the security of never putting the principal at risk. **This is very sophisticated investing** that cannot be accomplished unless you have millions of dollars to deposit in a top world U.S. bank.

Ex. 499 at "Private Member Material and Manual" at unnumbered p. 5 (emphasis in original). In addition, TIGC's description of the "trading programs" to which they had access also confirms the existence of investor pooling: "These 'trading' programs are run by a very tight knit inner circle that requires an invitation by the right person and a large amount of cash, for you to get even a hint of what is transpiring." Ex. 499 at "TIGC Private Member Manual" at 1.

Defendants only object to the second aspect of horizontal commonality, *i.e.*, that profits and losses are shared on a *pro rata* basis among investors. They argue that because the investment contracts were fixed at either 138% or 181%, investors did not share *pro rata* in profits and losses.

Defendants' argument fails in three respects. First, the Supreme Court stated in *Howey* that "[t]he definition of a security embodies a flexible rather than a static principle, one that is capable of adaptation to meet the countless and variable schemes devised by those who seek the use of the money of others on the promise of profits." *Howey*, 66 S.Ct. at 1103; *see also Tcherepnin v. Knight*, 389 U.S. 332, 338, 88 S.Ct. 548, 554 (1967). In other words, the duck theory applies: if it looks, reads, and sounds like an investment contract, it is an investment contract. TIGC's get-rich-without-risk scheme certainly is such a duck.

Second, defendants' claim that investors do not share "*pro rata*" in TIGC's gains and losses because of TIGC's fanciful guarantees of principal and profit is unavailing because, as Chief Judge Posner so pungently put it, "[i]t would be a considerable paradox if the worse the securities fraud, the less applicable the securities laws." *SEC v. Lauer*, 52 F.3d 667, 670 (7th Cir. 1995). In order to accept defendants' contention, we would have to endorse the fiction of complete guarantee and zero risk littered throughout TIGC's materials. This record – in which TIGC never earned one penny's return on at least $11.9 million invested – simply will not support such an endorsement.

Third, and more importantly, even if we were to accept defendants' argument that the definition for horizontal commonality should be narrowly and literally construed, we still find it to be present here. Dictionary definitions of standard English usage confirm that *pro rata* means "in proportion to the value or extent (of his interest)." XII *Oxford English Dictionary* 529 (2d ed. 1989).

Black's Law Dictionary defines *pro rata* as "proportionately; according to a certain rate, percentage, or proportion." *Id.* at 1220 (6th ed. 1990). Such percentages are trumpeted throughout TIGC's materials: either 138% or 181%, depending on how much is invested. *Pro rata* does not imply, as defendants appear to believe, that the investors' shares must be equal or variable. If our Court of Appeals had so intended, it might have used the term *per capita*, which Black's defines as "by the heads or polls . . . share and share alike." *Id.* at 1136. Thus, horizontal commonality is present in this investment scheme.

Lastly, the Commission has proven element three of *Howey*, *i.e.*, that the investors were led to believe that profits on their moneys would be generated solely from the efforts of TIGC's trustees and employees. By constructing in their offering materials a Wonderland of international finance, into which only they, and not the uninitiated Alice, could step through the looking glass, defendants encouraged investors to commit their money to TIGC's treasury and then rely exclusively on TIGC's investment efforts. For example, TIGC's "Financial Resources Special Report," page two, provides that "[y]ou will never have to sell anything to anyone. Never buy any products that you don't want. Never recruit. And you will still make a good profit." *Id.* Page six of that report is even more unequivocal, assuring the prospective investor that he or she need only send TIGC a check and "you are guaranteed 100% that you will make a profit . . . [*sic*] Even if you do nothing else you will be earning money right from the start." *Id.*

We have little trouble, therefore, finding that the Commission has met *Howey*'s definition of an investment

contract, and thus TIGC's investment offerings were securities within the meaning of the 1933 and 1934 Acts. Defendants' suggestion that we do not have jurisdiction over this subject matter is therefore without merit.

An Order follows.

IN THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF PENNSYLVANIA

SECURITIES AND EXCHANGE COMMISSION	:	CIVIL ACTION
v.	:	
THE INFINITY GROUP COMPANY, et al.	:	NO. 97-5458

ORDER

AND NOW, this 5th day of February, 1998, upon consideration of "defendants' motion to dismiss plaintiff's complaint for lack of subject matter jurisdiction", which we shall treat as a suggestion of lack of subject matter jurisdiction pursuant to Fed. R. Civ. 12(h)(3), and for the reasons cited in the accompanying Memorandum, it is hereby ORDERED that the "motion" is DENIED.

BY THE COURT:

/s/ Stewart Dalzell, J.
Stewart Dalzell, J.

IN THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF PENNSYLVANIA

SECURITIES AND EXCHANGE COMMISSION	:	CIVIL ACTION
Plaintiff,	:	
v.	:	
THE INFINITY GROUP COMPANY, et al.	:	
Defendants,	:	
and	:	
FUTURES HOLDING COMPANY, et al.	:	No. 97-5458
Relief Defendants.	:	

ORDER FOR A FINAL INJUNCTION, DISGORGEMENT, AND OTHER RELIEF

AND NOW, this 6th day of February, 1998, after a final injunction hearing in this matter held on February 2, through 5, 1998, and in accordance with the findings of fact and conclusions of law announced from the bench and as definitively issued as a Memorandum today, including this Court's findings that:

(a) This Court has jurisdiction over the subject matter of this action and over the defendants, relief defendants and each of them, and venue properly lies in this District;

(b) The Commission has made a sufficient and proper showing in support of the relief granted herein, as required by Section 20(b) of the Securities Act, 15 U.S.C. § 77t(b), and Section 21(d) of the Exchange Act, 15 U.S.C.

§ 78u(d), by establishing by a preponderance of the evidence that the defendants, and each of them, directly or indirectly, have engaged in and, unless enjoined by order of this Court, will continue to engage in acts, practices, and courses of business constituting violations of Sections 5(a), 5(c), and 17 (a) of the Securities Act, 15 U.S.C. §§ 77e(a), 77e(c), and 77q(a), Section 10(b) of the Exchange Act, 15 U.S.C. § 78j(b), and Rule 10b-5 promulgated thereunder, 17 C.F.R. § 240.10b-5, it is hereby ORDERED that:

1. Defendants and their officers, agents, servants, employees, attorneys, successors-in-interest, and those persons in active concert or participation with them who receive actual notice of this Order by personal service or otherwise, and each of them, are PERMANENTLY ENJOINED from violating Section 17(a) of the Securities Act, 15 U.S.C. § 77q(a), directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails, or of any facility of any national securities exchange, to

a. employ any device, scheme, or artifice to defraud;

b. obtain money or property by means of any untrue statement of a material fact or any omission to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading; or

c. engage in any transaction, practice, or course of business which operates or would operate as a fraud or deceit upon a purchaser, in connection with the offer or sale of any security;

2. Defendants and their officers, agents, servants, employees, attorneys, successors-in-interest, and those persons in active concert or participation with them who receive actual notice of this Order by personal service or otherwise, and each of them, are PERMANENTLY ENJOINED from violating Section 10(b) of the Exchange Act, 15 U.S.C. § 78j(b), and Rule 10b-5, 17 C.F.R. § 240.10b-5, promulgated thereunder, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails, or of any facility of any national securities exchange, to

a. employ any device, scheme, or artifice to defraud;

b. make any untrue statement of a material fact or omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading; or

c. engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person, in connection with the purchase or sale of any security;

3. Defendants and their officers, agents, servants, employees, attorneys, successors-in-interest, and those persons in active concert or participation with them who receive actual notice of this Order by personal service or otherwise, and each of them, are PERMANENTLY ENJOINED from violating Sections 5(a) and 5(c) of the Securities Act, 15 U.S.C. §§ 77e(a) and (c), by, directly or indirectly, in the absence of any applicable exemption:

a. making use of any means or instruments of transportation or communication in interstate commerce or of the mails to sell the securities of any issuer, through the use or medium of any prospectus or otherwise, unless and until a registration statement is in effect as to such securities; or

b. carrying or causing to be carried through the mails or in interstate commerce, by any means or instruments of transportation, for the purpose of sale or for delivery after sale, the securities of any issuer, unless and until a registration statement is in effect as to such securities;

4. Robert F. Sanville, C.P.A. ("Sanville"), shall continue as trustee for all funds, assets, choses in action, or other property belonging to, in the possession of, beneficially owned by, or in the control of TIGC, and in furtherance of his duties, Sanville, as trustee, shall:

a. take custody, control and possession of all funds, assets, choses in action, and other property of TIGC, including funds and other assets frozen by our Order of September 5, 1997, and assume all rights and powers which TIGC had or may have to manage, control, operate, maintain, possess or receive such assets;

b. take such action as is necessary and appropriate to prevent the dissipation or concealment of any assets, or as necessary for the preservation of any assets, including:

(i) making such payments and disbursements from the funds so taken into his custody, or

thereafter received, as necessary for the preservation of any asset;

(ii) sell, lease, or otherwise liquidate any non-cash assets of TIGC and deposit the proceeds received into the account(s) maintained for this matter;

(iii) pursue such causes of action as deemed necessary and appropriate and in the interest of the estate to recover assets of TIGC, or assert any right on behalf of investors who purchased securities from defendants, provided that twenty-four hours' advance notice is given to this Court of such causes of action;

(iv) trace TIGC's assets and investigate the books, records and accounts of TIGC; and

(v) hold all assets of TIGC, including all investor checks currently in TIGC's possession or received by Sanville, pending final determination of their disposition as may be further ordered by this Court;

c. As soon as practicable, notify all existing TIGC investors of the terms of this order, initiate proof of claim procedures in order to determine the Trust's final obligations to its investors;

d. provide to the Court, by March 9, 1998, a report detailing

(i) the choses in action which the Trustee intends to pursue, the funds and other assets which the Trustee intends to recover in each action, and the estimated attorneys' fees and costs of litigation for those actions,

(ii) the Trustee's progress in distributing proof of claim forms to investors, or otherwise determining the Trust's obligation to its investors; and

(iii) any funds or other assets received or disbursed since January 16, 1998, the date of the Trustee's last accounting;

e. be entitled to reasonable compensation from the assets now held by or in the possession, custody or control of, or which may be received by, defendants. Such compensation shall be in amounts commensurate with the services performed by the trustee and those he employs, shall be requested on a monthly basis with full documentation and support, and shall be subject to the approval of the Court;

5. a. Defendants, relief defendants and their officers, directors, subsidiaries, agents, servants, employees, attorneys, successors-in-interest, and those persons in active concert or participation with them who receive actual notice of this Order by personal service or otherwise, and each of them, SHALL DISGORGE to Sanville, the TIGC Trustee, funds or assets now held by them, under their control or over which they exercise actual or apparent investment or other authority, in whatever form such funds or other assets may now exist, and wherever located, in amounts up to and including the amounts of:

(i) $24,597,386.29, in joint and several liability, from defendants TIGC, Geoffrey P. Benson, and Geoffrey J. O'Connor;

(ii) $2,488,515.94, in joint and several liability, from SLB Charitable Trust and Susan L. Benson;

(iii) $1,425,900.00, in joint and several liability, from Futures Holding Company and Susan L. Benson;

(iv) $125,000.00, in joint and several liability, from JGS Trust and Susan L. Benson;

(v) $1,265,000.00 from Lindsey K. Springer, d/b/a Bondage Breaker Ministries;

b. Any financial or brokerage institution or other person or entity located within the territorial jurisdiction of the United States courts and holding any funds, accounts or other assets in the name, for the benefit or under the control of defendants, relief defendants, or any of them, or are signatories or have signing authority, an which receives actual notice of this Order by personal service or otherwise, SHALL DISGORGE to Sanville, the TIGC Trustee, any funds or other assets in such accounts;

6. Any brokerage institution, bank, savings and loan, mutual fund, or any other person, partnership, or corporation maintaining or having custody or control of any brokerage or deposit account or other assets of defendants or relief defendants under their control, and that receives actual notice of this Order by personal service or otherwise, shall, within three business days of receipt of that notice, serve on Sanville, the TIGC Trustee, a statement setting forth, with respect to each such account or other asset, the balance in the account or description of the assets as of the close of business on the date of receipt of the notice. Service of such statement on the TIGC Trustee shall be by express courier service or telefax directed to Robert F. Sanville, Trustee, The Infinity Group

Company Trust, P.O. Box 717, Abington, PA, 19001-0717 (telephone no. (215) 885-7930, telefax no. (215) 884-8686);

7. Defendants, relief defendants and each of them, shall fully cooperate with Sanville in the performance of his duties, provided that nothing in this Order shall be construed to require defendants to abandon any constitutional or other legal privilege which they may have available to them. Such cooperation shall include the production of the following records to Sanville:

a. All securities, funds, real estate, and other assets held in his, her, or its name, or in which he, she, or it has had any direct or indirect beneficial interest, stating the location of each of the assets;

b. each account with any financial institution or brokerage firm maintained in his, her, or its name, or in which he, she, or it has or has had any direct or indirect beneficial interest;

c. the address of each location from which he, she, or it has done business or received funds or assets from investors, or any other person;

d. every transaction in which any funds or other assets of any kind were transferred between or among himself, herself, or itself and any other defendant(s) or relief defendant(s) in this action, or from him, her, or it to any other person or to any entity in which any of the defendants or other persons have any ownership interest;

e. all funds received from investors, or any other person, including a list of:

(i) the name, address, and telephone number of each investor; and

(ii) the amount invested by each investor and a statement of the location and disposition of any funds received from investors or other person;

f. all currency transactions or other transaction constituting or relating to the investment of funds raised from investors;

g. all transactions relating to the leveraging of funds raised from investors; and

h. the names, addresses and telephone numbers of all present and former employees, officers, directors, agents, attorneys, representatives, associates, affiliates, or subsidiaries of defendants and relief defendants;

9. Defendants, relief defendants and their officers, agents, servants, employees, attorneys, successors-in-interest and those persons in active concert or participation with them who receive actual notice of this Order by personal service or otherwise, and each of them, are PERMANENTLY RESTRAINED from destroying, mutilating, concealing, altering, or disposing of any document referring or relating in any manner to (i) the acts, practices and transactions described in the Commission's Complaint in this action; (ii) communications between or among any of the defendants and/or their employees or agents; (iii) funds received from investors, or any other person; or (iv) the location and disposition of funds received from investors, or any other person. As used in this Order, "document" means the original and all non-

identical copies (whether non-identical because of handwritten notation or otherwise) of all written, graphic, audio, or video matter, however produced, and any other tangible record, or electronic data compilation capable of reproduction in tangible form, including, without limitation, telephone answering machine or other audiotapes, videotapes, correspondence, memoranda, minutes, telephone records, reports, studies, telexes, diaries, calendar entries, contracts, and letters of agreement, and including any and all existing drafts of all documents;

10. Pending final distribution of the TIGC assets by the Trustee, defendants TIGC, Geoffrey P. Benson, and Geoffrey J. O'Connor, and relief defendants Susan L. Benson, Futures Holding Company, JGS Trust, SLB Charitable Trust, Lindsey K. Springer and Bondage Breaker Ministries, their agents, officers, servants, employees, attorneys, and those persons in active concert or participation with them who receive actual notice of this Order by personal service or otherwise, and each of them, be and hereby are RESTRAINED and ENJOINED from filing a petition in bankruptcy without first notifying this Court, the Trustee, and the Commission by express courier service or telefax, five business days before such filing;

11. The Commission is granted leave to make application for civil penalties against defendants when and if defendants have made full remission of the disgorgement ordered herein

12. The Clerk shall enter this Order and Final Injunction as a final judgment, as no just reason for delay exists within the meaning of Fed. R. Civ. P. 54(b); and

13. The Clerk shall CLOSE this matter statistically.

BY THE COURT:

/s/ Stewart Dalzell, J.
Stewart Dalzell, J.

UNITED STATES COURT OF APPEALS
FOR THE THIRD CIRCUIT

Nos. 98-1215, 98-1216, 98-1217

UNITED STATES SECURITIES AND
EXCHANGE COMMISSION,

v.

THE INFINITY GROUP COMPANY; GEOFFREY P. BENSON; GEOFFREY J. O'CONNOR; FUTURES HOLDING COMPANY; SLB CHARITABLE TRUST; SUSAN L. BENSON; JGS TRUST; LINDSAY SPRINGER; BONDAGE BREAKER MINISTRIES

LINDSAY SPRINGER; BONDAGE BREAKER MINISTRIES,

THIRD-PARTY PLAINTIFFS

v.

THE UNION STATES OF THE CONSTITUTION, i.e.; ALASKA; ALABAMA; ARKANSAS; ARIZONA; CALIFORNIA; COLORADO; CONNECTICUT; DELAWARE; FLORIDA; GEORGIA; HAWAII; IOWA; ILLINOIS; INDIANA; KANSAS; KENTUCKY; LOUISIANA; MASSACHUSETTS; MARYLAND; MAINE; MICHIGAN; MINNESOTA; MISSOURI; MISSISSIPPI; MONTANA; NORTH CAROLINA; NORTH DAKOTA; NEBRASKA; NEW HAMPSHIRE; NEW JERSEY; NEW MEXICO; NEVADA; NEW YORK; OHIO; OKLAHOMA; OREGON; PENNSYLVANIA; RHODE ISLAND; SOUTH CAROLINA; SOUTH DAKOTA; TENNESSEE; TEXAS; UTAH; VIRGINIA; VERMONT; WISCONSIN; WEST VIRGINIA;

WYOMING; WASHINGTON; FEDERAL STATE DISTRICT OF COLUMBIA,

THIRD-PARTY DEFENDANTS

Geoffrey J. O'Connor (98-1215), Geoffrey P. Benson (98-1216), Susan L. Benson, Pro Se on behalf of herself in her representative capacity on behalf of SLB Charitable Trust, Futures Holding Company and JGS Trust (98-1217),

Appellants

SUR PETITION FOR REHEARING

BEFORE: BECKER, *Chief Judge*
SLOVITER, MANSMANN, SCIRICA, NYGAARD, ALITO, McKEE, BARRY, FUENTES, AMBRO
Circuit Judges
and SCHWARTZ, *Senior District Judge**

The petition for rehearing filed by the Appellant in the above-entitled case, having been submitted to the judges who participated in the decision of this court and to all other available circuit judges in regular active service, and no judge who concurred in the decision having asked for rehearing, and a majority of the circuit judges in regular active service not having voted for rehearing by this court en banc, the petition for rehearing is hereby **DENIED.**

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*The Honorable Murray M. Schwartz, Senior District Judge of the United States District Court for the District of Delaware, vote is limited to panel rehearing.

IT IS SO ORDERED.

By the Court,

/s/ Theodore A. McKee
Hon. Theodore A. McKee
Circuit Judge

DATED: 14 JUL 2000